STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

In the matter of XO Illinois, Inc.	)	
	)	
Petition for Arbitration Pursuant to	)	
Section 252(b) of the Telecommunications	)	**Docket No. 01-0466**
Act of 1996 to Establish an Interconnection	)	
Agreement with Illinois Bell Telephone	)	
Company d/b/a Ameritech Illinois	)	

DIRECT TESTIMONY

OF

ERIC L. PANFIL

On Behalf of
AMERITECH ILLINOIS

July 26, 2001

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Eric L. Panfil. My business address is 225 W. Randolph St, Chicago, Illinois 60606.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Illinois Bell Telephone Company (Ameritech Illinois) as Director - Network Technology and New Services in the Illinois Regulatory organization.

Q. WHAT ARE YOUR DUTIES AND RESPONSIBILITIES IN THAT POSITION?

A. I am responsible for policy development and advocacy on a broad range of regulatory matters, with particular focus on issues related to network technology, network interconnection, and the evolution and development of competitive networks and services.

Q. HOW LONG HAVE YOU BEEN IN YOUR PRESENT POSITION?

A. I have been in my present position since October 2, 2000. Prior to accepting this new position, I was employed by Ameritech Corporation as Director - Local Exchange Competition Issues, where I was responsible for issue analysis and policy development across all aspects of the evolving competitive environment for local exchange services in both the state and federal jurisdictions, with a focus on network interconnection issues.

Q. PLEASE DESCRIBE YOUR PROFESSIONAL BACKGROUND AND EXPERIENCE IN THE TELECOMMUNICATIONS INDUSTRY RELEVANT TO YOUR TESTIMONY.

A. I have been a member of the Regulatory and Public Policy Organizations at Ameritech (including its predecessor and subsidiary companies) since 1982, when I assumed responsibility for development of interexchange carrier switched access tariffs. At various times since, I have been responsible for policy development, issues analysis, tariff development, tariff interpretation, rate and cost development, demand analysis, and imputation analysis for carrier switched access (in both the federal and state jurisdictions), cellular carrier interconnection, payphone service, competitive carrier interconnection, and network unbundling. Prior to 1982, I worked in the Information Systems Department, where I held program design and coding, systems design, project management, and software support management positions.

I have testified in Illinois on behalf of Ameritech Illinois on numerous occasions over the past 15 years, most recently in Consolidated Dockets 97-0404, 97-0519, and 97-0525, which were complaint proceedings regarding the applicability of reciprocal compensation arrangements to ISP traffic under the terms of certain interconnection agreements, and in Dockets 00-0027 and 00-0332, the arbitrations between Ameritech Illinois and Focal Communications and Level 3 Communications respectively. In addition, I have testified in proceedings before the Indiana, Michigan, Ohio, and Wisconsin Commissions on numerous issues, primarily in the area of network interconnection for LEC, wireless, and interexchange carrier networks, and the related inter-carrier compensation arrangements.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN THIS PROCEEDING?

A. The purpose of my direct testimony is to address Ameritech Illinois's position in response to XO's arbitration petition filed on June 25, 2001. I will address first and foremost Ameritech Illinois's position on compensation for Local and ISP traffic. In addition, I will explain why Ameritech Illinois feels the terms and conditions of the entire Reciprocal Compensation Appendix are legitimately related, and therefore should be renegotiated due to the FCC's *ISP Compensation Remand Order*[1] issued on April 18, 2001.

Q. DOES XO DISPUTE AMERITECH ILLINOIS'S CONTENTION THAT IT MAY NOT OPT-IN TO THE PROVISIONS OF THE FOCAL AGREEMENT FOR INTERCARRIER COMPENSATION IN THE XO SUCCESSOR ILLINOIS AGREEMENT?

A. No. In Mr. Kinkoph's testimony XO concedes it cannot opt into the ISP intercarrier compensation provisions of the Focal-Ameritech Illinois interconnection agreement (the "Focal Agreement"). (Verified Statement of Douglas W. Kinkoph at 3, lines 21-24.)

Q. DID XO MAKE A PROPOSAL FOR THE RATES, TERMS AND CONDITIONS FOR ISP AND OTHER INTERCARRIER COMPENSATION IN THE XO SUCCESSOR ILLINOIS AGREEMENT?

A. Yes. XO's proposed language, as it appears in Appendix E to XO's Petition, is as follows:

> 4.7 Compensation for the transport and termination of Local Traffic and IntraLATA Toll Traffic shall be pursuant to this Section 4.7. The

[1] *In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Intercarrier Compensation for ISP-Bound Traffic ("ISP Compensation Remand Order")*, CC Dockets 96-98 and 99-68, FCC 01-131, Opinion and Order Adopted April 18, 2001, 2001 WL 431687.

Reciprocal Compensation arrangements set forth in this Section 4.7 are not applicable to (i) Exchange Access traffic, (ii) traffic terminated to Requesting Carrier using Ameritech's unbundled switching and for which the Requesting Carrier incurs no incremental cost to terminate traffic, (iii) traffic originated by one Party on a number ported to its network that terminates to another number ported on that same Party's network or (iv) any other type of traffic found to be exempt from Reciprocal Compensation by the FCC or the Commission. All Exchange Access traffic and IntraLATA Toll Traffic shall continue to be governed by the terms and conditions of applicable federal and state tariffs. Compensation for traffic that is delivered through Transit Service shall be pursuant to Section 7.2.

4.7.1 Reciprocal Compensation applies for transport and termination of Local Traffic billable by Ameritech or Requesting Carrier which a Telephone Exchange Service Customer originates on Ameritech's or Requesting Carrier's physical switch for termination on the other Party's physical switch. The originating Party shall compensate the terminating Party for the transport and termination of Local Traffic for the function(s) provided by that terminating Party at the rate(s) provided at Item II of the Pricing Schedule (i.e. End Office Local Termination, Tandem Switching, Tandem Transport Termination, and Tandem Transport Mileage). The Parties' obligation to pay Reciprocal Compensation to each other shall commence on the date the Parties agree that the network is complete (i.e., each Party has established its originating trunks as well as any ancillary functions (e.g., 9-1-1)) and capable of fully supporting originating and terminating Customer (and not a Party's test) traffic.

4.7.2 Each Party shall charge the other Party its effective applicable federal and state tariffed intraLATA FGD switched access rates for those functions a Party performs relating to the transport and termination of IntraLATA Toll Traffic.

4.7.3 Compensation for transport and termination of all traffic which has been subject to performance of INP by one Party for the other Party pursuant to Article XIII shall be as specified in Section 13.7.

:

Q. DID AMERITECH ILLINOIS MAKE A PROPOSAL FOR THE RATES, TERMS AND CONDITIONS FOR ISP AND OTHER INTERCARRIER COMPENSATION IN THE XO SUCCESSOR ILLINOIS AGREEMENT?

A. Yes. Although I did not personally negotiate with XO and its representatives, I can verify that the Appendix Reciprocal Compensation filed with Ameritech Illinois's

Response in this docket is Ameritech's proposal on ISP and other intercarrier compensation with XO in Illinois. By way of background, I understand that XO first proposed adopting the Focal Agreement on or about May 30, 2001, which was well after the negotiations for a successor contract in Illinois had begun. In response, on July 5, 2001, Ameritech Illinois forwarded its counterproposal, which consisted of a complete Appendix Reciprocal Compensation consistent with the requirements of the FCC's *ISP Compensation Remand Order*. That Appendix provided a comprehensive set of rates, terms and conditions governing intercarrier compensation for ISP-bound traffic as well as for all other traffic exchanged between XO and any SBC Communications Inc.-owned Incumbent LEC, including Ameritech Illinois. I understand that one of XO's complaints was that the July 5th version of Appendix Reciprocal Compensation was overbroad and included terms specific to other SBC-owned ILECs, such as Southwestern Bell and Pacific Bell Telephone Company. Ameritech Illinois therefore struck any non-Ameritech terms from the Appendix Reciprocal Compensation, and provided a revised Appendix to XO on July 19, 2001. This revised Appendix Reciprocal Compensation, with some additional, for the most part non-substantive, modifications, was attached to Ameritech Illinois's Response to XO's Petition for Arbitration in this case. As I understand it, XO has shown no inclination to accept the Appendix Reciprocal Compensation in any of the versions Ameritech Illinois has offered.

Q. WHY CAN'T XO SIMPLY ADOPT THE FOCAL AGREEMENT'S TERMS AND CONDITIONS ON RECIPROCAL COMPENSATION, AND APPLY THEM TO ISP COMPENSATION?

A. The *ISP Compensation Remand Order* prohibits XO from adopting provisions of the Focal Agreement that relate to inter-carrier compensation on ISP-bound traffic. There, the FCC clarified the jurisdictional classification ISP and other Internet-bound traffic, and stated :

> *Because we now exercise our authority under section 201 to determine the appropriate intercarrier compensation for ISP-bound traffic, however, state commissions will no longer have authority to address this issue. For this same reason, as of the date this Order is published in the Federal Register, carriers may no longer invoke section 252(i) to opt into an existing interconnection agreement with regard to the rates paid for the exchange of ISP-bound traffic [footnote omitted].* [2]

Because compensation for ISP-bound traffic is no longer subject to section 252(i) MFN rules, the parties must meet, confer, and exchange proposals in good faith negotiations over the appropriate terms and conditions for ISP traffic in the Agreement. Ameritech Illinois attempted to meet some of XO's concerns in its revised Appendix Reciprocal Compensation filed in this case. XO's Petition and proposal on ISP compensation, however, seem to suggest that XO believes it may force Ameritech Illinois to take whatever terms and conditions it selects for reciprocal compensation for ISP traffic. XO does not appear to contemplate that any discussion could be had as to the compensation terms found in the Focal Agreement. ISP compensation and all legitimately related terms and conditions are by federal mandate now subject to negotiation. XO has rejected Ameritech Illinois's proposed Appendix Reciprocal Compensation out of hand, and has not redlined the document or provided specific counterproposals of any kind.

---

[2] ISP Compensation Remand Order, para 82 (emphasis added).

Accordingly, with the time for negotiation of the parties' agreement allotted by the 1996 Act having passed, the matter is now before this Commission.

Q. WHAT RATES DOES AMERITECH ILLINOIS PROPOSE FOR TRAFFIC EXCHANGED WITHIN THE LOCAL CALLING SCOPE?

A. Ameritech Illinois's proposal, set forth in section 5.0 of the Appendix Reciprocal Compensation, is that the parties should compensate each other for call termination at *bifurcated* rates that – unlike XO's proposed rates – properly take into account the unique cost characteristics of both *call set-up* and *call duration*, and that therefore more accurately reflect, in conformity with section 252(d)(2) of the 1996 Act, the actual costs that the carrier being compensated incurs for transporting and terminating individual calls.

Q. WHY IS AMERITECH ILLINOIS PROPOSING A BIFURCATED RATE STRUCTURE FOR RECIPROCAL COMPENSATION?

A. The current rate structure causes many service providers to be systematically over-compensated or under-compensated for the transport and termination of local telecommunications traffic on their networks. These rates are in conflict with the FCC's rules and are therefore in many cases not "just and reasonable" as required by Section 252 of the federal Telecommunications Act. The problem is particularly acute in the typical arrangement where a CLEC is permitted to adopt "symmetrical" reciprocal compensation charges based on the rates of an ILEC with which it is interconnecting,

Q. WHAT IS THE SOURCE OF THIS PROBLEM WITH THE RATE STRUCTURE?

A. In simple terms, it is a problem of costs being "averaged" in a manner that does not reflect the potential for different providers to have traffic characteristics (and therefore cost characteristics) that vary dramatically from the average. The per-minute rates developed for the current reciprocal compensation rate elements are actually a composite of two separate cost streams. It is universally understood and accepted in the telecommunications industry that the cost of switching and transporting a call includes both costs that are incurred only once per call (generally called "setup cost") and costs that continue to accrue for the duration (number of minutes of hold time) of the call (generally referred to as "duration cost"). Historically, in the design of reciprocal compensation rates (just as for the switched access rates which were the model for the reciprocal compensation rate structure) those two types of costs have been melded into a simpler per-minute cost, since it was assumed that hold times were relatively stable, and would not vary significantly from carrier to carrier. For example, when Ameritech Illinois's cost studies for reciprocal compensation end office switching rates were originally developed in 1996, the setup and duration costs were melded based on an assumed duration of about 3.5 minutes per call. The result (using the slightly revised "compliance" version of those costs filed in April 1998) was a switching rate of $.003746, which included the setup cost ($.009512 per message) spread over each of the 3.5 minutes (as an addition to a duration cost of $.000967 per minute). The tandem switching rate element also has identified cost components that are setup-related and others that are duration-related.

However, the experience of the last few years has taught us that for local calls, hold times are not at all stable, and average overall hold times vary dramatically from provider to provider. Over the last few years, the nature of the traffic on the networks of local service providers has changed dramatically, driven primarily by the explosion in Internet access traffic on the local voice networks. Internet access calls originating on Ameritech Illinois's network have an average duration of about 26 minutes per call, according to our most recent traffic study (October 1999), and the average duration of such calls has been increasing over time (in the first such study performed by Ameritech in March, 1997, the average duration of Internet access calls in Illinois was 22.6 minutes). Applying the current per-minute rate to a 26-minute call results in recovery of the proper amount of duration cost but recovers over *six times* the setup cost.

Q. BUT DON'T MOST LOCAL SERVICE PROVIDERS HANDLE A VARIED MIX OF CALL TYPES, SO THAT THEIR OVERALL TRAFFIC CHARACTERISTICS ARE SIMILAR TO THE OVERALL CHARACTERISTICS OF AMERITECH ILLINOIS'S TRAFFIC?

A. Unfortunately (and understandably, given the economic incentives provided by the current rate structure), that is not the case. Numerous CLECs have incoming traffic characteristics such that the average hold time for all of the calls delivered to their networks by Ameritech Illinois exceeds 20 minutes per call.

This huge disparity in traffic characteristics results from the opportunity that CLECs have to selectively market their services to particular types or classes of customers. Under the current rate structure for reciprocal compensation, customers such as providers of Internet access service, providers of chat line services, and businesses offering work-at-home access to their corporate networks, all of which generate incoming

calls with hold times substantially longer than typical local calls, are particularly attractive customers for competitive local service providers because the compensation paid on those types of calls significantly exceeds the cost incurred.

Q. YOU STATED EARLIER THAT THE CURRENT RATE STRUCTURE IS NOT IN CONFORMANCE WITH THE FCC'S RULES. WHAT ARE THE FCC'S RULES REGARDING THE RATE STRUCTURE FOR RECIPROCAL COMPENSATION?

A. The FCC's specific rule for the rate structure of reciprocal compensation for the transport and termination of local telecommunications traffic is in Section 51.709, and reads as follows:

> **§ 51.709 Rate structure for transport and termination.**
>
> (a) In state proceedings, a state commission shall establish rates for the transport and termination of local telecommunications traffic that are structured consistently with the manner that carriers incur those costs, and consistently with the principles in §§ 51.507 and 51.509 of this part.

Sections 51.507 and 51.509 (which specifically set forth the rules for pricing of unbundled network elements) provide no additional specifics regarding the appropriate rate structure for reciprocal compensation, but also require as an initial matter that "rates shall be structured consistently with the manner in which the costs . . . are incurred."

This rule is grounded in a very sound policy analysis by the FCC, which recognized that reciprocal compensation rates that depart from cost causation principles would create incentives for economically inefficient and narrow competitive entry, rather than the broad-based, economically efficient competitive environment envisioned by the federal Telecommunications Act. That is exactly what has happened under the current non-cost-based rate structure – competitive local service providers have focused almost exclusively on the few niche customer groups and services that provide them with the

opportunity to receive excessive compensation through arbitrage of a uneconomic rate structure.

Q. WHAT ARE THE PROVISIONS OF THE TELECOMMUNICATIONS ACT THAT THE FCC'S RULES FOR THE RATE STRUCTURE FOR RECIPROCAL COMPENSATION ARE INTENDED TO IMPLEMENT?

A. The Act itself includes the following standard for the pricing of reciprocal compensation:

> SEC. 252.
> * * *
> (d) PRICING STANDARDS-
> * * *
> (2) CHARGES FOR TRANSPORT AND TERMINATION OF TRAFFIC-
> (A) IN GENERAL- For the purposes of compliance by an incumbent local exchange carrier with section 251(b)(5), a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless--
> (i) such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier; and
> (ii) such terms and conditions determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls.

Plainly, rates that do not conform with the FCC's rule would not be just and reasonable under the Act, as they would not represent a reasonable approximation of the additional costs of terminating such calls.

Q. WHY ARE THE CURRENT RATES IN ILLINOIS NOT IN CONFORMANCE WITH THE FCC'S RULES REGARDING THE RATE STRUCTURE FOR RECIPROCAL COMPENSATION?

A. Ameritech Illinois's current reciprocal compensation rates in Illinois (and also the rates of all other local service providers (i.e., CLECs and wireless carriers) that use those same rates under the FCC's "symmetrical rates" rule) are inconsistent with the requirement that

they be "structured consistently with the manner that the carriers incur those costs." Given the wide variation in average hold times among all of the local service providers that use Ameritech Illinois's rates, a rate structure that recovers per-call setup costs on a per-minute basis is not consistent with the FCC rule. Even as applied to Ameritech Illinois itself, given the continuing rapid changes in traffic characteristics on the local network, rates that result from the averaging of setup and duration cost components based on an assumed duration per call cannot reasonably be judged to be consistent with the FCC rule, particularly when it is such a simple matter to fix the problem with an easily implemented modification of the rate structure.

Q. WHAT IS THE SOLUTION?

A. The solution to this problem is simply to apply a two-part rate structure consisting of separate per-call and per-minute rates to all traffic for which reciprocal compensation is applicable under the Commission's and the FCC's current policies. The two-part rate structure would be implemented for each rate element for which separate setup and duration costs have been identified in the cost studies that form the basis for Ameritech Illinois's current reciprocal compensation rates.

Q. WHAT ARE THE COSTS APPROVED BY THE COMMISSION, AND WHAT ARE THE CURRENT RATES BASED ON THOSE COSTS?

A. The TELRIC cost studies that form the basis for the current reciprocal compensation rates were submitted to Staff in March of 1998 in compliance with the Second Interim Order in Docket Nos. 96-0468/0569 Consolidated (the "TELRIC Docket"). However,

those cost studies actually date for the most part to September, 1996, when tariffs and supporting cost studies were filed by Ameritech Illinois. The Commission's investigation of those costs (among many others) in the TELRIC Docket resulted in changes to certain basic factors, such as fill factors, economic, lives, and cost of capital, affecting all TELRIC cost elements, but did not change any of the more granular elements of the studies such as the identification of cost elements as being setup-related or duration-related. Ameritech Illinois filed rates in conformance with those "compliance" costs on April 3, 1998, and those rates became effective on April 18, 1998. Those rates were developed based on an "average per-minute" rate structure for reciprocal compensation, and are as follows:

End Office Switching	$0.003746 per MOU
Tandem Switching	$0.001072 per MOU
Tandem Transport Termination	$0.000201 per MOU
Tandem Transport Facility Mileage	$0.000013 per MOU per Mile

Q. FOR WHICH RATE ELEMENTS DO THE COSTS THAT SUPPORT THE CURRENT RECIPROCAL COMPENSATION RATES INCLUDE SEPARATE COST COMPONENTS FOR SETUP AND DURATION?

A. In reviewing the cost study results, I find that those costs include separate setup and duration components for two elements: end office switching and tandem switching.

Q. WHAT RATES WOULD RESULT FROM THOSE COSTS IN THE BIFURCATED RATE STRUCTURE PROPOSED BY AMERITECH ILLINOIS?

A. Based on those costs, and with the addition of NVS shared and common costs using the factors mandated by the Commission for use with those costs, Ameritech Illinois's proposed restructured rates would be:

	Rate per Call	Rate per MOU
End Office Switching	$0.009512	$0.000967
Tandem Switching	$0.000496	$0.000927
Tandem Transport Termination	(none)	$0.000201
Tandem Transport Facility Mileage	(none)	$0.000013 per Mile

As shown in the above chart, only the End Office Switching and Tandem Switching rates would change; the Tandem Transport Termination and Tandem Transport Facility Mileage rates would remain unchanged.

Q. HOW ARE THE COSTS SEPARATED INTO SETUP AND DURATION COMPONENTS IN ORDER TO CREATE BIFURCATED RATES?

A. The process is very simple and straightforward. It is essentially a matter of "un-doing" the averaging step that was performed at the end of the TELRIC analysis, just before the NVS shared and common cost factor was applied to produce the rate. The original cost studies clearly identify which costs are setup (per-call) costs and which costs are duration (per-minute) costs. The setup (per-call) costs include switch equipment, measurement, SS7, and billing. As a final "averaging" step in those studies, the setup costs were divided by the assumed average hold time per call (slightly under 3.5 minutes in the case of the cost studies at issue here) and were added to the true duration costs in order to produce a per-minute cost/rate that would recover both setup and duration costs, provided that the assumption regarding the average hold time per call turned out to be accurate. In order to create bifurcated rates, one must simply take the setup and duration cost components identified in the original study, and apply the Commission-approved NVS shared and common cost factors directly to those costs.

Panfil Schedule 1, attached to this testimony, shows the detailed cost components for End Office and tandem switching, and demonstrates how both the averaged rates and the corresponding bifurcated rates are calculated.

Q. IS AMERITECH ILLINOIS PROPOSING THAT THE COMMISSION DIRECT THE PARTIES TO USE THESE BIFURCATED RATES FOR TRAFFIC THAT IS SUBJECT TO RECIPROCAL COMPENSATION UNDER SECTION 251(b)(5) OF THE 1996 ACT, OR FOR ISP-BOUND TRAFFIC, OR FOR BOTH?

A. Ameritech Illinois believes that in this proceeding, the Commission should require the parties to exchange 251(b)(5) traffic at the proposed bifurcated rates. Those rates would then potentially apply as well to ISP-bound traffic by operation of the FCC's *ISP Compensation Remand Order*.

Q PLEASE EXPLAIN.

A. First, the FCC's Order states, at paragraph 82, that the states no longer have authority to regulate inter-carrier compensation on ISP-bound traffic. Accordingly, Ameritech Illinois is not asking the Commission to rule on the rates at which the parties compensate each other on ISP-bound traffic.

Under the FCC's Order, however, Ameritech Illinois is required to exchange ISP-bound traffic at the same rates as 251(b)(5) traffic until such time, if any, as Ameritech Illinois chooses to avail itself of the rate caps that the FCC's Order establishes for ISP-bound traffic. (FCC Order ¶ 78.) Consequently, whatever rates the Commission requires the parties to use for 251(b)(5) traffic will also potentially apply to ISP-bound traffic – not because this Commission will so require, but because the FCC has so ruled.

Q. WHAT IF AMERITECH ILLINOIS DOES AT SOME POINT ELECT TO AVAIL ITSELF OF THE RATES THAT THE FCC'S ORDER ESTABLISHES FOR ISP-BOUND TRAFFIC?

A. Under the FCC's Order, Ameritech Illinois, in order to exercise its right to exchange ISP-bound traffic at the capped rates established in the Order, must offer to exchange all 251(b)(5) traffic with all local service providers (i.e., CLECs and wireless carriers, as well as other ILECs) in Illinois at the same rates. If Ameritech Illinois at some point makes such an offer, it is highly likely, for reasons I explain below, that some carriers will accept, and others will decline. Ameritech Illinois would then exchange ISP-bound traffic with all carriers at the capped rates established by the FCC (which it would be entitled to do by virtue of having offered to exchange all 251(b)(5) traffic at the same rates). Ameritech Illinois would also then exchange 251(b)(5) traffic at those same capped rates with some carriers, namely, carriers that accepted Ameritech Illinois's offer to do so. With other carriers, however (those who declined the offer), Ameritech Illinois would find itself exchanging 251(b)(5) traffic at the (presumably higher) rates for such traffic approved by this Commission. I of course do not know how XO would respond to an Ameritech Illinois offer to exchange all 251(b)(5) traffic at the FCC's capped rates.

Q. YOU SAID THAT IF AMERITECH ILLINOIS WERE TO OFFER TO EXCHANGE ALL 251(b)(5) TRAFFIC AT THE CAPPED RATES ESTABLISHED IN THE FCC'S ORDER, SOME CARRIERS WOULD ACCEPT AND OTHERS WOULD DECLINE. WHY DO YOU BELIEVE THAT IS SO?

A. I would expect each carrier to respond to such an offer by Ameritech Illinois in the way that best serves that carrier's economic interests. Assume, for the sake of illustration, that the Commission-approved reciprocal compensation rates for 251(b)(5) traffic are higher than the FCC caps. In that scenario, those carriers that terminate more Ameritech

Illinois-originated 251(b)(5) traffic than they originate for termination on the Ameritech Illinois network would refuse the offer, because they would benefit by exchanging traffic at the higher state rate. On the other hand, carriers that originate more 251(b)(5) traffic than they terminate would accept the offer, because they would benefit financially by exchanging traffic at the lower FCC rate.

Q. WHAT BEARING DOES THIS HAVE ON AMERITECH ILLINOIS'S PROPOSAL FOR BIFURCATED RATES?

A. The FCC's Order, though in many respects reasonable and appropriate, in effect requires Ameritech Illinois, as a pre-condition to availing itself of the FCC's capped rates for ISP-bound traffic, to offer all local carriers in Illinois the opportunity to engage in arbitrage. The arbitrage opportunity lies in each carrier's choice to exchange 251(b)(5) traffic at either higher or lower rates (as I explained in the preceding answer), depending on the characteristics of the traffic it exchanges, and, for that matter, to target particular classes of customers or particular classes of traffic in order to maximize the benefit of exchanging such traffic at the higher or lower rates it has chosen. This arrangement is obviously economically inefficient, because it encourages carriers to base their business plans not on their ability to provide services economically, but on their ability to take advantage of an anomaly in the inter-carrier compensation rate structure. Also, of course, the arrangement is a losing proposition for Ameritech Illinois, which would wind up exchanging 251(b)(5) traffic at higher rates with "heavy terminating" carriers and at lower rates with "heavy originating" carriers.

Q. HAVE OTHER STATE COMMISSIONS ADDRESSED THIS ISSUE AND FOUND THAT RECIPROCAL COMPENSATION RATES SHOULD BE STRUCTURED WITH SEPARATE SETUP AND DURATION CHARGES?

A. Other states have recognized the need to match rates more closely to cost characteristics. In a January 23, 2001 Order in Docket U-12696, the Michigan PSC approved a change to bifurcated rates proposed by Ameritech Michigan, stating (at page 7):

> The Commission finds that Ameritech Michigan's proposal for changing the rate structure for reciprocal compensation should be adopted. Ameritech Michigan's showing that a rate structure predicated upon dual charges for per-call setup and per-minute usage better reflects cost causation has not been rebutted by the other carriers.

Similarly, the Public Service Commission of Wisconsin, in its Order in Docket 05-TI-283, concluded (at page 13) :

> The Commission finds it is reasonable to eliminate the assumption regarding call length from the calculation. Instead, the cost associated with setting up a call (e.g., establishing a circuit, and creating a billing record) should be recovered once per call, in the first minute of the call. There would be a duration charge for the first minute of the call as well. During subsequent minutes, the only cost recovered would be that associated with duration, or the cost to maintain the circuit and transmit the content of the call.

In addition, reciprocal compensation rates in Pacific Bell's interconnection agreements in California have included separate setup and duration prices since 1996, first on an interim basis, and subsequently with TELRIC rates officially adopted by the California PUC in November 1999. Texas, as a result of a proceeding last year, established a structure in which bifurcated reciprocal compensation rates would apply to all minutes that exceed a 3-to-1 balance ratio between two local service providers, which was generally believed to include most of the long-duration traffic such as Internet access traffic.

Q. IS INTERNET ACCESS TRAFFIC THE ONLY TYPE OF TRAFFIC THAT CAN CAUSE AVERAGE HOLD TIME CHARACTERISTICS TO VARY AMONG LOCAL SERVICE PROVIDERS?

A. No. In addition to the chat line and work-at-home data network types of traffic that I mentioned earlier, other types of traffic may have significantly different hold time characteristics (though not as extreme as those for ISP-bound traffic). Business local calls tend to have shorter durations on average than residential calls, so a carrier serving primarily business customers may have traffic characteristics different from those of the industry as a whole. The same may also be true of wireless voice (cellular and PCS) traffic.

Q. WHY DOES AMERITECH ILLINOIS CONTEND THAT TERMS OTHER THAN THE RATES FOR ISP TRAFFIC ARE LEGITIMATELY RELATED TO THE RECIPROCAL COMPENSATION APPENDIX?

A. Ameritech Illinois believes that the *ISP Compensation Remand Order* requires the parties to negotiate and address more than just the rate to be applied to ISP traffic. Other compensation-related terms such as switch recordings, Calling Party Number (CPN) signaling, and billing are all legitimately related to the rates themselves, and must be negotiated in order to develop a complete and serviceable agreement. The physical realities of interconnection further dictate that more than just rates be discussed. ISP traffic is exchanged on the same interconnection trunk groups as all other local traffic being traded between the networks. Local interconnection trunk groups may carry combined Local and IntraLATA toll traffic, even though different rates apply to those two categories of traffic. Similarly, the switch recordings that capture the minutes of use on those combined Local and IntraLATA Toll trunk groups will be recording both the ISP and voice traffic flowing between the networks. The parties therefore must come to

some understanding of how the parties will jurisdictionalize the ISP traffic, and properly rate the different classes of traffic.

Q. WHY IS IT NECESSARY THAT THE AGREEMENT ADDRESS RATES FOR ISP TRAFFIC EXCHANGED OUTSIDE OF THE LOCAL CALLING SCOPE?

A. Because it is possible that "non-local" ISP traffic will be exchanged between the networks. The FCC's *ISP Compensation Remand Order* addresses the appropriate compensation obligations that apply when calls are delivered from one LEC's end user customer to an ISP in the same local calling area that is served by a competing LEC.[3] However, the FCC was very specific in the remand, making it clear that services enumerated under 251(g) were not subject to reciprocal compensation, and that Congress did not intend to disrupt the pre-existing access regimes.[4] Future interconnection agreements must contain language that accurately reflects the intent of the FCC as discussed in the *ISP Compensation Remand Order*.

Q. PLEASE DESCRIBE HOW END USERS COULD DIAL AN ISP CALL THAT MIGHT FALL UNDER THESE INTER OR INTRASTATE ACCESS REGIMES?

A. End users may access the Internet a number of different ways. Other than dialing a local number, end users may access their ISP provider by dialing an 800 number, or via Foreign Exchange service. Although not as common, end users may, dial 1+ and incur inter or intraLATA toll charges to access the Internet. In the Reciprocal Compensation Appendix, Ameritech Illinois is proposing language that specifically addresses the

---

3 See *ISP Compensation Remand Order*, ¶ 13.

4 See *ISP Compensation Remand Order*, ¶ ¶ 36 and 37.

appropriate intercarrier compensation mechanism for each of these scenarios. The language XO is proposing contains no such explanations, and risks operational or billing disputes in the future.

Q. PLEASE SUMMARIZE HOW AMERITECH ILLINOIS'S PROPOSED APPENDIX WILL JURISDICTIONALIZE ISP CALLS?

A. The Appendix Reciprocal Compensation Ameritech Illinois is proposing contains specific terms governing how ISP traffic is jurisdictionalized during the life of the interconnection agreement. Unlike the language XO would have this Commission adopt, Ameritech Illinois's proposed language clearly identifies that Calling Party Number (CPN) call signaling shall be the preferred method of distinguishing between local and transit traffic, intraLATA toll and switched access traffic. For example, Section 5.5 of the proposed Appendix Reciprocal Compensation states:

> All ISP- and Internet-bound traffic shall be subject to the same terms and conditions regarding switch recordings, Calling Party Number (CPN) signaling, and other usage detail as for other Local Calls under this Appendix. Minutes of use to ISPs may be shown separately on the monthly usage detail, invoices, payment summaries, or other documents exchanged between ILEC and CLEC in the monthly billing cycle.

Similarly, Ameritech also includes the appropriate citation to the billing of non-local ISP traffic exchange:

> 8.0 INTRALATA 800 TRAFFIC – Refer to Section VII.3.9 of the Underlying Agreement
>
> 9.0 MEET-POINT-BILLING (MPB) and SWITCHED ACCESS TRAFFIC COMPENSATION – Refer to Article VI of the Underlying Agreement
>
> 10.0 INTRALATA TOLL TRAFFIC COMPENSATION
>
> 10.1 For intrastate intraLATA toll traffic, compensation for termination of intercompany traffic will be at terminating access rates for Message Telephone Service (MTS) and originating access

> rates for 800 Service, including the Carrier Common Line (CCL) charge where applicable, as set forth in each Party's Intrastate Access Service Tariff, but not to exceed the compensation contained in an ILEC's tariff in whose exchange area the End User is located. For interstate intraLATA intercompany service traffic, compensation for termination of intercompany traffic will be at terminating access rates for MTS and originating access rates for 800 Service including the CCL charge, as set forth in each Party's interstate Access Service Tariff, but not to exceed the compensation contained in the ILEC's tariff in whose exchange area the End User is located. Common transport, (both fixed and variable), as well as tandem switching and end office rates apply only in those cases where a Party's tandem is used to terminate traffic.

Since ISP-bound traffic is intermingled with these other forms of traffic for purposes of rating and routing, it is necessary to renegotiate the entire appendix rather than assume that only limited portions (such as the rates) are affected. XO's proposal does not make these important clarifying distinctions, and should not be adopted.

Q. ARE OTHER PORTIONS OF THE APPENDIX RECIPROCAL COMPENSATION SPECIFIC TO ISP TRAFFIC?

A. Yes. Ameritech Illinois proposes that the parties clarify that other portions of the interconnection agreement regarding local interconnection trunking, meet point billing (exchange access) trunking, and other network concepts be identified as applicable to ISP traffic, such as proposed section 6.3:

> Physical interconnection, routing, and trunking of ISP calls on an Inter-Exchange basis, either IntraLATA or InterLATA, shall be as specified in the Agreement for all other traffic exchanged, including but not limited to, the need to route over Meet Point Billed trunks.

Q. HAVE YOU EXPLAINED IN THIS TESTIMONY WHY EACH PROVISION IN AMERITECH ILLINOIS'S PROPOSED APPENDIX RECIPROCAL COMPENSATION SHOULD BE ADOPTED?

A. I have focused intensively on the most important provisions, and have explained in

general terms why the Appendix as a whole should be adopted. I have not, however, undertaken to provide support for every individual provision in the Appendix, because I do not know at this point whether XO actually objects to each individual provision. (While XO has declined to accept the Appendix in its entirety, I do not take that to mean that XO has objections to every individual provision in the Appendix.) To the extent that the testimony that XO files in response to this testimony offers criticisms of provisions I have not focused on, I will address those criticisms in my rebuttal testimony. And if Staff has questions about any provisions in the Appendix, I hope I will be given the opportunity to address those questions, either at hearing or by way of a response to a Data Request.

Q. WHAT IF STAFF WERE TO TAKE THE POSITION THAT WHILE AMERITECH ILLINOIS'S PROPOSAL – THE BIFURCATED RATES IN PARTICULAR – HAS MERIT, THE COMMISSION SHOULD CONSIDER THE PROPOSAL IN A PROCEEDING IN WHICH ALL CLECS CAN PARTICIPATE, INSTEAD OF IN THIS PROCEEDING?

A. Ameritech Illinois believes that the Commission should address the question of bifurcated rates, and the Appendix Reciprocal Compensation in its entirety, in this proceeding. The 1996 Act establishes two-party arbitrations as the means – the only means – by which CLEC and ILEC arrive at terms and conditions to implement the substantive requirements of section 251 of the Act, and that includes reciprocal compensation. Under the 1996 Act, therefore, this section 252(b) arbitration is the proper forum for determining the rates at which XO and Ameritech Illinois will compensate each other for the transport and termination of section 251(b)(5) traffic, and the terms and conditions that will apply to the parties' reciprocal compensation arrangements.

There may be rare circumstances where a state Commission, almost of necessity,

defers an arbitration issue to a generic proceeding. In the first generation of arbitrations in Illinois, for example, the Commission decided to split off all rate issues into a separate "TELRIC" proceeding, and to have the arbitrating parties pay each other proxy rates pending the outcome of that proceeding. By doing so, the Commission enabled all CLECs to participate in a single cost docket, and also allowed itself the time it felt it needed to thoroughly examine the complex pricing issues with which it was presented.

Here, however, Ameritech Illinois's core proposal, the bifurcated rates, is, really, a rather simple proposal, and it can and should be dealt with thoroughly and fairly in this proceeding.

Q. HOW WOULD YOU RESPOND TO A SUGGESTION THAT THE COMMISSION DIRECT THE PARTIES TO USE AMERITECH ILLINOIS'S CURRENT (TARIFFED) RECIPROCAL COMPENSATION RATES DURING THE INITIAL PART OF THE TERM OF THEIR INTERCONNECTION AGREEMENT, BUT SUBJECT TO CHANGE, WITH A POSSIBLE RETROACTIVE TRUE-UP, DEPENDING ON THE OUTCOME OF A GENERIC INQUIRY INTO AMERITECH'S RECIPROCAL COMPENSATION RATES?

A. Again, Ameritech Illinois believes that the record in this case will make clear beyond any doubt that the proposed bifurcated rate structure is an improvement over the current rate structure, and that the Commision should therefore approve the Appendix Reciprocal Compensation now, in this proceeding. At a bare minimum, though, if the Commission believes it necessary to ensure that the rates as between XO and Ameritech Illinois will ultimately match the rates as between other CLECs and Ameritech Illinois, Ameritech Illinois would then propose that the Commission, instead of taking the approach

suggested in the question, direct the parties to exchange traffic at the proposed bifurcated rates from the outset, but subject to change, with a possible true up, in the event that the Commission should arrive at a different conclusion later.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes it does.

Original Analysis	Illinois End Office	Illinois Tandem
Setup Related		
Bill Processing & Rendering	$0.005038	$0.000000
Bill Inquiry (Service Center)	$0.000644	$0.000000
Total Non-Network Message Expenses	$0.005682	$0.000000
Switching and/or Transport Eqpt	$0.000756	$0.000345
Measurement (Recording)	$0.000075	$0.000000
SS7	$0.000104	$0.000000
Setup Cost per Message	$0.006617	$0.000345
Average Minutes per Message	3.424	3.424
Setup per Minute	$0.001933	$0.000101
Duration Related		
Switching and/or Transport Eqpt	$0.000673	$0.000645
Duration Cost per Minute	$0.000673	$0.000645
Total Setup + Duration Related		
Average Cost per Minute	$0.002606	$0.000746
NVS, Shared & Common Cost Factor	43.75%	43.75%
NVS, Shared & Common Costs per Minute	$0.001140	$0.000326
Composite Rate per Minute	$0.003746	$0.001072

New Analysis	Illinois End Office	Illinois Tandem
Setup Related		
Bill Processing & Rendering	$0.005038	$0.000000
Bill Inquiry (Service Center)	$0.000644	$0.000000
Total Non-Network Message Expenses	$0.005682	$0.000000
Switching and/or Transport Eqpt	$0.000756	$0.000345
Measurement (Recording)	$0.000075	$0.000000
SS7	$0.000104	$0.000000
Setup Cost per Message	$0.006617	$0.000345
NVS, Shared & Common Cost Factor	43.75%	43.75%
NVS, Shared & Common Costs per Minute	$0.002895	$0.000151
Total Setup Rate per Message	$0.009512	$0.000496
Duration Related		
Switching and/or Transport Eqpt	$0.000673	$0.000645
Duration Cost per Minute	$0.000673	$0.000645
NVS, Shared & Common Cost Factor	43.75%	43.75%
NVS, Shared & Common Costs per Minute	$0.000294	$0.000282
Total Duration Rate per Minute	$0.000967	$0.000927